Before the FEDERAL COMMUNICATIONS COMMISSION Washington, D.C. 20554

In the Matter of	
Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements) WC Docket No. 02-112

REPLY COMMENTS OF SBC COMMUNICATIONS INC.

TERRI L. HOSKINS
GARY L. PHILLIPS
SUZANNE YELEN
PAUL K. MANCINI

WILEY REIN & FIELDING LLP 1776 K Street, NW Washington, D.C. 20006 (202) 719-7000 – phone (202) 719-7049 - facsimile SBC COMMUNICATIONS INC. 1401 Eye Street, NW Suite 400 Washington, D.C. 20005 (202) 326-8891 – phone (202) 408-8763 – facsimile

Its Attorneys

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SUMMARY

Ignoring the language and legislative history of the Act, CLECs ask the Commission to rewrite the Act and impose new conditions on Bell operating companies (BOCs) before the existing restrictions are allowed to sunset. Most blatantly, several CLECs argue that the Commission should extend the Section 272 requirements until the BOCs have achieved a certain level of local market share or have been declared non-dominant. There is no basis for doing so. Congress rejected this approach, and the Commission has concluded dominance does not demonstrate a need for structural separation. Similarly, the CLECs' attempt to put the burden on BOCs to show that the requirements should sunset is backwards. Congress presumed that Section 272 would no longer be necessary three years after a BOC affiliate obtains Section 271 approval unless the Commission extends it, and Chairman Powell has made clear that those proposing a rule must show a clear and demonstrable justification. Further, the statute itself and its legislative history make clear that Congress intended for the sunset to occur on a BOC-by-BOC, not a state-by-state, basis, and no party has shown otherwise.

CLEC claims that BOCs are not complying with their obligations under the Act are unfounded. These allegations are exaggerated and inaccurate, and, more importantly, are unrelated to Section 272. For example, claims that BOC special access services have declined in quality and that BOCs are discriminating and cross-subsidizing services are incorrect. With increasing competition in this market, BOCs have every incentive to maintain high levels of services, and SBC has included quality measures and standards in its tariffs. This competition, in conjunction with the ease of detection, Section 272(e)(1), and BOC special access reports, prevents discrimination. In addition, price cap regulation and the Commission's accounting rules, including the affiliate transaction rules, are effective safeguards against cross-subsidization. Other alleged violations, such as PIC freeze discrimination, collocation enforcement actions, performance measures penalties, and tariffs, are irrelevant to Section 272, which governs BOC entry into the long distance market. The issues commenters raise are

governed by other provisions of the Act and Commission rules and will be unaffected by the Section 272 sunset.

Other claims for continuing Section 272's requirements are also misplaced. Extending the sunset simply to allow additional biennial audits is unnecessary. In addition, arguments that Section 272(c)(1)'s procurement requirements are still necessary are unwarranted. All this provision does is put BOCs at a disadvantage vis-à-vis their competitors. Finally, even with the Section 272 sunset, state and federal regulators will continue to have the enforcement authority necessary to ensure that BOCs meet their obligations under the Act.

CLEC claims that sunset should be continued because the costs of Section 272 are minimal are incorrect. SBC, Verizon, and BellSouth have shown that these requirements impose substantial burdens and disadvantage BOCs, particularly in the provision of complex services to large business customers and in the ability to take advantage of new integrated equipment. The OI&M restrictions are responsible for a large proportion of the increased costs and should be eliminated for all BOCs immediately. They are not required by the Act, and experience has shown they are unnecessary to ensure the independence of the BOC from its Section 272 affiliate. Other safeguards will prevent any anti-competitive behavior at a far lower cost.

Therefore, SBC urges the Commission to allow the Section 272 requirement to sunset three years after a BOC affiliate obtains Section 271 authority, as intended by Congress.

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Separate Affiliate and Related Requirements)	

REPLY COMMENTS OF SBC COMMUNICATIONS INC.

SBC Communications Inc., on behalf of itself and its subsidiaries (collectively referred to as "SBC"), hereby respectfully submits its reply to comments on the Notice of Proposed Rulemaking¹ adopted by the Federal Communications Commission ("Commission") in the above-captioned docket. As SBC showed in its Comments, Section 272 structural separation requirements impose significant costs and serve no useful purpose. While they are ostensibly designed to prevent discrimination and cross-subsidization, there is little, if any, risk in the real world that a Bell operating company (BOC) could derive market advantages through either form of anti-competitive behavior without detection. Cross-subsidization concerns have been obviated by price cap regulation, which severs the link between costs and rates. Moreover, Chairman Powell recently announced that the Commission would table reform of its accounting rules, so those rules will continue to provide "belt and suspenders" protection against any risk of cross-subsidization. Likewise, the risk of undetected discrimination is trivial for a whole host of reasons, including the inescapable fact that for discrimination to serve any purpose it must be evident to consumers, and if it is evident to consumers it surely will be evident to the BOCs' competitors and regulators as well.

As Chairman Powell has stated:

if we don't have a clear and demonstrable justification of a rule, then the appropriate role of government is to take the rule away or not interfere in the otherwise proper functioning of a market, rather than leave a rule in for good

¹ Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements, WC Docket No. 02-112, Notice of Proposed Rulemaking, 17 FCC Rcd 9916 (2002).

measure. Over history a lot of rules that were left for good measure ... have secondary effects that often harm the welfare of consumers. ... I don't think you've got to prove to me that a rule is not necessary. I think I have to prove that it is necessary. And if I can't do that, I don't think that I should intervene.²

These words are particularly apt in this proceeding. Although commenters serve up their usual dose of rhetoric, the reality is that none presents any compelling reason to postpone the sunset date established by Congress for structural separation. To the contrary, the only practical result of such an action would be to handicap the BOCs in the long-distance market, thereby distorting competition and denying consumers the benefits of an effectively functioning market. Indeed, that is precisely what those who propose extending these requirements have in mind. To avoid this result, SBC urges the Commission to allow the Section 272 obligations to sunset as scheduled and on a BOC-by-BOC basis, as provided in the Act.

I. CLECS' REWRITING OF SECTION 272 SHOULD BE REJECTED.

Section 272(f)(1) states that "[t]he provisions of this Section [272] (other than subsection (e)) shall cease to apply with respect to the manufacturing activities or the interLATA telecommunications services of a BOC three years after the date such BOC or any BOC affiliate is authorized to provide interLATA telecommunications services under § 271(d) unless the Commission extends such three-year period by rule or order." The BOCs' competitors, not surprisingly, urge the Commission to extend the three-year sunset date period so that the BOCs can compete less effectively in the long-distance market. They present no basis, however, for the Commission to trump the three-year sunset established in the Act.

A. Section 272 Does Not Include A Local Market-Share Or Non-Dominance Test.

Several parties argue that the Commission should extend the Section 272 requirements until CLECs have achieved a certain level of market penetration or until the BOCs are found to be non-dominant.⁴ AT&T, for example, claims that "[i]n evaluating whether to allow the Section

² "Powell defines stance on telecom competition," COMMUNICATIONS DAILY, May 22, 2001 at 2-3.

³ 47 U.S.C. § 272(f)(1).

⁴ See, e.g., NARUC at 4; WUTC at 2.

272 requirements to sunset, therefore, the core consideration, as it was when Section 272 was enacted, must be market power." Similarly, WorldCom contends that "the Commission should find that the stricter Section 272 separate affiliate requirements remain necessary as long as the BOCs remain dominant"

Certain other parties propose even stricter tests. The New Jersey Division of Ratepayer Advocate argues that the Commission should adopt a multifactor analysis that requires the BOC to demonstrate that it lacks market power by making *ten* separate showings. Similarly, Sprint argues that sunset should occur only after: (1) the Commission has adopted performance measurements and enforcement mechanisms for UNEs and special access; (2) three years have passed from the date on which the BOC obtains Section 271 authority in its last state; and (3) the BOC has shown compliance with Section 272 in two biennial audits in each of its states. Sprint suggests that after each of these conditions is fulfilled, the Commission can then consider whether the BOC is still dominant in the local and exchange access markets. Only if the BOCs are non-dominant will the Section 272 restrictions will be allowed to expire.

These tests have no basis in law or policy. Congress did not include a market share or multifactor tests for the Section 272 sunset, and for good reason. The mere fact that a carrier is classified as dominant in no way demonstrates the need for structural separation requirements. The Commission quite properly rejected that notion fifteen years ago, when it lifted *Computer II* structural separation requirements for AT&T and the BOCs. Significantly, the Commission found structural separation to be unnecessary notwithstanding that AT&T and the BOCs were dominant in their respective markets; indeed, the BOCs were not only dominant, but retained

⁵ AT&T at 10.

⁶ WorldCom at 3. Similarly, Time Warner claims that "[t]he Commission should retain Section 272 affiliate requirements until a BOC is non-dominant in the provision of special access and has substantially diminished ability to unilaterally raise prices for local exchange service in a state." Time Warner at 31. *See also* Focal Comments at 5.

⁷ NJ Division of Ratepayer Advocate at 8-9.

⁸ Sprint at 16-17.

franchised monopolies for local service. Moreover, price caps had not yet been implemented. Even more significant is that the Commission turned out to be correct. The lifting of Computer II structural separation requirements did not result in rampant or widespread discrimination or cross-subsidization, as had been predicted by the competitors of AT&T and the BOCs. Nonstructural safeguards proved wholly satisfactory even in the context of franchised monopolies and rate-of-return regulation, and even though – unlike the BOCs' long-distance competitors, which include large, established carriers that routinely and expertly monitor virtually every aspect of the access services they receive - the BOCs' enhanced services competitors were largely fledgling companies. Against this backdrop, it is evident that the real agenda of the BOCs' competitors is not to prevent discrimination and cross-subsidization; those concerns are mere pretexts. Rather, their real agenda is to saddle the BOCs with cost and other restraints that will prevent the BOCs from competing as effectively. The Commission should reject that cynical agenda and make clear that competitors should fight their battles in the marketplace, not by seeking unwarranted regulatory advantages. According to some CLECs, the three-year sunset should be extended because local competition has not developed as Congress expected. Even if these CLECs were right about competition – which they are not – their claims would be irrelevant for the reasons discussed above. It is simply not correct, as these CLECs assert, that possession of market power is an excuse for any and all regulatory constraints. Just as their "more is better" approach to unbundling is wrong, so too is their "more is better" approach when it comes to regulations that apply uniquely to their competitors.

In any event, the CLECs are wrong in their assertion that competition has not taken hold as Congress intended. Although they are fond of citing stale and incomplete data regarding local competition when such data serves their purposes, there is significant intramodal and intermodal local competition today. This competition is thoroughly documented in the UNE Fact Report submitted in the *Triennial Review* proceeding. As shown therein, CLECs serve at least 16% of

the nation's access lines and, most likely 20% of those lines, using their own facilities. ⁹ In addition, incumbent LECs face growing competition from providers of wireless and broadband services as well as cable telephony providers. As a result of this competition, wireline local voice traffic is declining for the first time in the history of modern telecommunications. Claims that competition has not developed in local markets are thus simply wrong.

To be sure, competition has centered around business customers and high-end residential customers who offer the highest margins. But that is only because those are the customers CLECs target, given the failure of state regulators to fulfill the critical statutory obligation of rebalancing local rates. The fact that retail rates for other customers are not high enough to attract competitive entry is hardly indicative of market power, much less a need for structural separation requirements.

As if all this were not dispositive, claims that Section 272 must be retained because local markets remain closed ignore that Section 271 authority is premised on the Commission's determination that the local exchange and exchange access markets are "irreversibly open" to competition. Thus, Section 271 authority *could not* be granted in a state if the markets in that state remains closed.

B. The Burden Of Proving That The Section 272 Requirements Should Not Sunset Falls On Those Advocating The Extension.

Some parties argue that the BOCs must bear the burden of demonstrating that there is sufficient competition to permit Section 272 obligations to sunset.¹⁰ For example, the New Jersey Division of the Ratepayer Advocate argues that for Section 272 to sunset "requires a BOC to demonstrate that it lacks market power."¹¹ Aside from the fact, demonstrated above, that the presence or absence of market power is not alone a basis for structural separation requirements,

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⁹ UNE Fact Report 2002, Prepared for and Submitted by BellSouth, SBC, Qwest, and Verizon, April 2002 at I-5, I-6.

¹⁰ See, e.g., NJ Division of Ratepayer Advocate at 8.

¹¹ NJ Division of Ratepayer Advocate at 8.

these arguments cannot be reconciled with the statute. Even if Congress had not established a presumption in favor of sunset, as it clearly has done, the BOCs would still not have the burden of proving that sunset is warranted. To the contrary, the Act reflects a preference for deregulation over regulation and requires the Commission to conduct a biennial review of all of its regulations and to eliminate those that are not necessary. To suggest that the BOCs must prove the need for deregulation is thus out of step with the crux of the Act. But it is not just the deregulatory thrust of the Act and the biennial review provisions that belie these arguments. Section 272 itself does. Section 272(f)(1) states that structural separation requirements will sunset unless the Commission extends them. Thus, the Act establishes a presumption that the structural separation requirements will sunset, and it is those who favor extending the sunset date that must overcome this presumption. No party has come close to meeting this burden.

C. The Act Requires That The 272 Safeguards Sunset On A BOC-by-BOC Rather Than A State-by-State Basis.

SBC demonstrated in its comments that both the plain language of the statute and its legislative history indicate that Congress intended for Section 272 to sunset on a BOC-by-BOC, rather than state-by-state, basis.¹² The House Bill originally provided that the requirements would sunset in eighteen months after interLATA entry "in such state." The Senate Bill, in contrast, adopted a case-by-case sunset to be administered by the Commission. The Conferees rejected both approaches and instead adopted a three-year application of Section 272 which "would commence on the date on which the BOC is authorized to offer interLATA services." Thus, Section 272 states that it shall cease to apply "[three] years after the date such BOC or any BOC affiliate is authorized to provide interLATA telecommunications services." BellSouth

¹² SBC at 19-21.

¹³ H.R. Rep. No. 104-22, at 7 (1995).

¹⁴ H.R. Conf. Rep. No. 104-458, at 152 (1995), reprinted in 1996 U.S.C.C.A.N. 164.

¹⁵ 47 U.S.C. § 272(f)(1).

and Verizon both analyze the statutory language and legislative history in detail and agree that Congress intended for Section 272 to sunset on a BOC-by-BOC basis.¹⁶

Sprint asks the Commission to rule that Section 272 obligations sunset "three years from the date on which an RBOC obtained Section 271 authority in the last of its states in which it is an ILEC." This argument cannot be squared with the text of Section 272(f)(1). The text provides that Section 272 requirements sunset when "a *Bell operating company or any Bell operating company affiliate* is authorized to provide interLATA telecommunications services." (emphasis added). Sprint would have the Commission change the word "any" to "all" and force the BOC to wait until it has received approval in every state before the Section 272 restrictions sunset. Once again, the Commission should reject this attempt to rewrite the Act.

II. CLAIMS THAT THE BOCS ARE NOT COMPLYING WITH THE ACT AND THAT BOCS CAN ENGAGE IN ANTI-COMPETITIVE BEHAVIOR ARE UNFOUNDED.

Commenters offer their usual litany of unsubstantiated, half-baked allegations that BOCs are violating the Act in one fashion or another. SBC responds to these allegations below simply to set the record straight. The important point, however, is that none of these claims – even if true – provides any basis for extending Section 272 requirements. In order for structural separation to be an appropriate response to allegations of misconduct, it must be shown, at a minimum, that structural separation would be an effective and appropriate check against the conduct claimed. None of the commenters even purports to make that showing, nor could they, frankly, since the violations they allege ostensibly took place notwithstanding the application of structural separation. In any event, as shown below, the allegations, at least as directed against SBC, are misleading and inaccurate. The most critical evidence of BOC compliance with Section 272 is the two Section 272 biennial audits. SBC's audit report shows that the independent auditor found only minor issues, and Verizon's audit report was similarly

¹⁶ BellSouth at 5-9; Verizon at 3-6.

¹⁷ Sprint at 4-6, 16.

favorable.¹⁸ Although some commenters argue that the few discrepancies noted by the auditors demonstrate noncompliance,¹⁹ the reports show that the auditors found no evidence of either discrimination or cross-subsidization. Further, although AT&T argues that the audits were not sufficiently thorough,²⁰ the extensive detail in the reports refutes this assertion.²¹

In addition, the significant safeguards already in place address any concerns about potential discrimination and cross-subsidization. The purpose of the Section 272 requirements is to prevent the BOCs from using their position in the local and exchange access markets to engage in anti-competitive behavior in the long distance market. Existing protections in the Act and the Commission's rules prevent any discrimination or cross-subsidization without the costs imposed by structural separation, a requirement Congress presumed would be temporary.

A. BOCs Are Neither Discriminating Nor Cross-Subsidizing In Their Provision Of Special Access Services.

Claims that BOC special access service performance has declined and that BOCs discriminate by providing better service to their retail customers than to CLECs²² are inaccurate. As an initial matter, parties present no evidence whatsoever that SBC has discriminated in its provision of special access services, much less that structural separation remains necessary to prevent such discrimination. The significant and growing competition for special access services is, in itself, an effective check against discrimination.²³ But even apart from this competition,

¹⁸ SBC at 15.

¹⁹ See, e.g., CompTel at 19-20.

²⁰ AT&T at 44.

²¹ See, e.g., SBC Communications Inc., Report of Independent Accountants on Applying Agreed-Upon Procedures, CC Docket No. 96-150 (filed December 2001).

²² CompTel at 7-9; AT&T at 24-29.

²³ As SBC has shown in numerous other proceedings, the special access market is subject to substantial competition. *See UNE Fact Report 2002*, submitted in Triennial Review Proceeding. *See, also, Performance Measurements and Standards for Interstate Special Access Services, et al.*, SBC Communications Inc. Comments, CC Docket No. 01-321 *et al.* at 8 (filed Jan. 22, 2002).

the Act contains safeguards that will remain in effect even after sunset. These safeguards include *inter alia* Section 272(e), which does not sunset with the rest of Section 272.

Because of the growing competition SBC faces in special access services, SBC strives to address the service quality needs of its wholesale special access customers. SBC works extensively with those customers on an operational level to identify and resolve service quality issues. As part of these efforts, SBC has made numerous process changes to better meet customer needs. SBC has also implemented various service quality measures and standards, as well as customer-specific performance reporting where requested to monitor service quality. As a result of these efforts, SBC's special access performance has improved during the past two vears.²⁴ Moreover, safeguards against discrimination and poor service quality already exist since SBC's standard special access tariffs contain performance measurements and penalties for missing certain targets, including targets relating to service installation on-time performance and service interruption. Furthermore, SBC has developed a contract-based tariff option, which contains additional, premium performance standards, and substantial liquidated damages if the performance standards are not met.²⁵ In light of SBC's demonstrated performance²⁶ and service improvement efforts, as well as existing safeguards, there is no basis for a claim that SBC is not complying with the Act, much less that any such violations require the continuation of structural separation requirements.

Several parties assert that removal of Section 272 obligations will allow BOCs to discriminate in the provision of special access services.²⁷ As SBC explained in its comments,

²⁴In its comments, AT&T incorrectly states in a footnote that the Texas Commission has initiated an investigation of SBC's special access performance. Rather, the Texas Commission is arbitrating whether to adopt performance measures, not, as AT&T misleadingly suggests, to investigate potential performance problems.

²⁵ See Performance Measurements and Standards for interstate Special Access Services, et al., SBC Communications Inc. Comments, CC Docket no. 01-321 et al. at 11 (filed Jan. 22, 2002).

²⁶ See SBC written ex parte filed August 23, 2002 in which SBC specifies its special access performance levels for critical areas of performance.

²⁷ See, e.g., WorldCom at 6; CompTel at 9; Texas PUC at 7-8.

numerous safeguards prevent BOCs from engaging in this or other anti-competitive behavior. First, competition in the access market is widespread and growing rapidly, with markets generating 80 % of BOC special access revenues qualifying for Phase I pricing flexibility and markets generating nearly two-thirds of such revenues qualifying for Phase II relief.²⁸ Second, any discrimination would be easily detectable by both competitors and regulators. Third, Section 272(e)(1), which does not sunset, requires that a BOC fulfill any requests for local or exchange access services for unaffiliated entities in a period no longer than it fulfills such services for itself and its affiliates. Fourth, the existing BOC reports provided under Section 272(e)(1) allow competitors and regulators to monitor BOC performance.²⁹ Thus, structural separation requirements are superfluous. AT&T asserts that elimination of structural separation will enable the BOCs to cross-subsidize long distance services with revenues from access and local services.³⁰ This is nonsense. As SBC explained in its comments, BOCs are subject to price cap regulation at both the state and federal level. Price cap regulation severs the link between regulated costs and prices.³¹

While price cap regulation is dispositive as to cross-subsidization claims, the Commission could seek additional protection by affording BOC long-distance operations nonregulated treatment for federal accounting purposes.³² The Commission concluded in the

²⁸ See Performance Measurements and Standards for interstate Special Access Services, et al., SBC Communications Inc. Comments, CC Docket no. 01-321 et al. (filed Jan. 22, 2002).

²⁹ SBC committed in each of its 271 applications as part of its compliance with Section 272(e)(1) to track the following: 1) Percentage Completion - Desired Due Date; 2) Promised Due Date to in service interval; 3) Firm Order Confirmation interval; 4) PIC Change implementation interval; 5) Time to Restore and trouble duration; 6) Time to restore PIC; and 7) Mean time to clear network.

³⁰ AT&T at 34-40.

³¹ SBC at 13. In addition, Section 272(e)(3), which requires that a BOC impute to itself an amount for local and exchange access services that is no less than the amount changed to unaffiliated carriers, remains in effect even after the sunset.

³² Accounting Safeguards Order, ¶ 75.

Accounting Safeguard Order that Part 64 "should sufficiently safeguard against cross-subsidization without imposing additional accounting requirements on carriers." Thus affording integrated interstate long distance services nonregulated treatment for Part 64 accounting purposes will provide an additional layer of protection to consumers. Part 64 also requires that BOCs file a cost allocation manual at least annually showing how the BOC is allocating costs and the methodology used³⁴ and mandates an independent audit. Thus, even after the Section 272 sunset, BOCs would be subject to similar accounting rules as under Section 272.

AT&T claims that the Part 64 rules are an insufficient substitute for Section 272 because "they are designed to measure services provided to end-users, not carrier-to-carrier services." To the contrary, Part 64 allocates costs for all services between regulated and nonregulated accounts, whether the service is provided to an end user or to a carrier. Incidental interLATA services under Section 271(g), provided on a carrier-to-carrier basis, are examples of services treated as non-regulated under Part 64.

AT&T further argues that the Commission found that Part 64 was not sufficiently detailed to satisfy Section 272(b). The Commission's Part 64 reference pertains to the affiliate transactions in Section V of the CAM and the need for more detailed affiliate transaction descriptions, not to the insufficiency of Part 64 in general. When Section 272(b) sunsets and long distance service is offered by the BOC on an integrated basis, Section V limitations will not apply because long distance service will be listed in Section II of the CAM as a nonregulated activity, for which there is revenue product reporting. Also, some states (such as California) require full product tracking of revenues and costs of nonregulated services. But, following

³³ *Id*.

³⁴ 47 C.F.R. § 64.903(b).

³⁵ AT&T at 51.

³⁶ *Id*.

sunset pursuant to the Act, whether Section 272's requirements are satisfied is irrelevant. Thus, AT&T is incorrect that the Part 64 rules are inadequate protection.

B. Other Claims Of BOC Non-Compliance Are Exaggerated And, In Any Event, Unrelated To Section 272.

AT&T also complains that BOCs use the PIC freeze process to discriminate.³⁷ AT&T's real complaint, however, is that it was unable to convince the Commission to deny BOC customers the ability to protect themselves from slamming through PIC freezes.³⁸ Thus, AT&T's arguments, once again, have nothing to do with the merits of structural separation. AT&T also asserts that BOCs are misallocating costs through inflated special access services rates and inaccurately priced transfers among affiliates.³⁹ As to AT&T's pending price squeeze complaint in Texas, these charges are baseless.⁴⁰ This is true as well for AT&T's assertion of discriminatory behavior in inter-affiliate transfers.⁴¹ Indeed, as explained above, price cap regulation at the state and federal level has eliminated any incentive or ability the BOCs once might have had to misallocate costs. In addition, the Commission's detailed accounting and cost allocation rules, including affiliate transactions rules that govern transfers between affiliates,

³⁷ AT&T at 29-32

³⁸ AT&T fails to mention in their comments that in some states, Michigan and Texas for some IXCs encourage their customers to place a PIC freeze on their account.

³⁹ AT&T at 34-40

⁴⁰ In Texas, AT&T filed a complaint against SWBT and SBC LD shortly after SBC received 271 relief, asking for reduction to cost of SWBT's intrastate switched access rates and claiming that SWBT's intrastate switched access rates and SBC LD's predatory prices created a price squeeze in the Texas long distance market. Following a ruling by the Texas PUC in favor of SWBT and SBC LD on the applicability of predatory pricing principles to the complaint, AT&T withdrew its predatory pricing claim. AT&T now claims that intra-corporate cross subsidization is causing the price squeeze. In 1999, the Texas Legislature set the level of intrastate switched access rates and also barred the PUC from subjecting, under any circumstances, a company that elected incentive regulation to a hearing, complaint, or determination regarding the reasonableness of its rates, revenues, rate of return, or net income. SWBT filed suit in state court to enjoin the Texas PUC from proceeding with an unlawful hearing. Just this past week, a District Court in Travis County, Texas enjoined the Texas PUC from further proceedings on almost all issues related to AT&T's complaint.

⁴¹ AT&T at 38. The CPUC 314.5 audit proceeding that AT&T references is still pending. SBC has taken issue with these allegations in the audit report and is confident that the CPUC will find that Pacific Bell is in compliance with the applicable CPUC and FCC requirements.

prevent any cost misallocation.⁴² Like Section 272, these rules also call for an independent audit to ensure BOC compliance.⁴³ Further, Section 272(e)(3), which requires that a BOC impute to itself an amount for local and exchange access services that is no less than the amount charged to unaffiliated carriers, remains in effect after the sunset.

CLECs offer numerous other ostensible gripes, including allegedly discriminatory tariff provisions, 44 Qwest/Touch America contract disputes, 45 and Commission enforcement actions on interconnection issues. 46 In addition, the Texas Public Utilities Commission states that because SBC has had to pay fines under its performance plan, the Section 272 requirements must be maintained, 47 and Sprint points to several Commission enforcement actions regarding collocation and digital subscriber line services. 48 However, none relates to Section 272 and delaying sunset would not affect these concerns. For example, Section 272 does not govern interconnection performance; it governs BOC entry into the long distance and manufacturing markets. Every BOC that has received Section 271 authority is subject to extensive detailed performance measures and self-enforcing penalty plans. 49 These plans, which include hundreds of measures

⁴² Although SBC has asked the Commission to relax its comprehensive accounting and reporting requirements, even these relaxed requirements would be effective in preventing cross-subsidization. *See* Joint Comments of BellSouth, SBC, Verizon, Qwest, Frontier, and CBT in Further Notice of Proposed Rulemaking in CC Docket Nos. 00-199, 99-301, and 80-286.

⁴³ In its *Computer III Order on Remand*, the Commission concluded that its nonstructural safeguards – including detailed cost allocation rules, submission of cost allocation manuals, independent audits, reporting requirements, an automated system to store and analyze submitted data, FCC performed on-site audits, and the adoption of price caps – were an effective alternative to structural separation in protecting against cross-subsidy.

⁴⁴ AT&T at 32-34.

⁴⁵ AT&T at 40-43.

⁴⁶ Sprint at 14-15.

⁴⁷ Texas PUC at 6.

⁴⁸ Sprint at 14-15.

⁴⁹ For example, pursuant to SBC's Section 271 approval in Arkansas and Missouri, on a monthly basis, SBC provided and continues to report information relative to over 700 total measurements (including principal measurements and disaggregated submeasurements).

and leave BOCs liable for millions of dollars in fines, will continue after Section 272 sunsets, giving state commissions and CLECs exactly the same protections against discrimination in the local market that they have today.

III. ADDITIONAL BIENNIAL AUDITS AND NONDISCRIMINATORY PROCUREMENT ARE UNWARRANTED.

The Texas and Wyoming Public Service Commissions' request that the Commission extends the Section 272 sunset to permit an additional biennial audit⁵⁰ is misplaced. Congress was well aware that the results of only one audit would be available prior to sunset.⁵¹ Maintaining the Section 272 requirements solely to allow additional audits that Congress declined to mandate would be an end-run around the statute.

WorldCom suggests that Section 272(c)(1), which prohibits BOC discrimination in the procurement of goods, services, facilities, and information, or in the establishment of standards, should be maintained because it represents "a more stringent standard' than the 'unjust or unreasonable' standard found in Section 202" and extends "to key non-common carrier services such as billing and collection." WorldCom's desire to subject the BOCs to special obligations provides no basis for doing so. No other competitor must solicit bids before selecting an IXC to provide a service. Requiring the BOCs to do this puts them at a substantial disadvantage vis-à-vis other carriers in providing bundled offerings. Further, WorldCom's reference to billing and collection highlights the unreasonableness of its argument. BOCs have been providing billing and collection services on an unregulated basis for over a decade and the Commission has consistently found that there is a competitive market for these services. The more flexible nondiscrimination standards in Sections 201 and 202 are all that is needed to ensure that all IXCs are competing on a level playing field.

⁵⁰ Texas PUC at 8; Wyoming PUC at 1.

⁵¹ While the results of the second audit period, covering the third year of a BOC's 271 authority, may not be available prior to sunset, the Commission maintains enforcement authority over the BOC to ensure compliance with the 272 requirements for this time period.

⁵² WorldCom at 7.

IV. FEDERAL AND STATE REGULATORS WILL CONTINUE TO HAVE THE ENFORCEMENT AUTHORITY TO ENSURE BOCS MEET THEIR OBLIGATIONS UNDER THE ACT.

The Texas Public Service Commission states that with the sunset of Section 272, "Texas is at risk of losing its only statutory means of monitoring SWBT's obligation to provide access to its network." The Texas Commission misunderstands the nature of Section 272. Section 272 governs BOC operations in the long distance market, not the local market. After sunset, the Texas Commission retains the same authority over BOC network access as it does today. The performance plan adopted by the Texas Commission to monitor SWBT's wholesale operations remains in place, as does the associated penalty mechanism. In addition, the Texas Commission will continue to conduct arbitrations and collaboratives.

Similarly, the Commission will continue to have the authority it needs to monitor BOC performance after the sunset. As noted above, the Section 272(e) obligations do not sunset and are subject to Section 271(d), which allows the Commission, among other penalties, to suspend or revoke Section 271 approval. In addition, the Commission has enforcement authority under Sections 4(i), 201, 202, 503, and 206-209 of the Act. Thus, sunset of the separation requirements does not diminish the Commission's enforcement options.

V. THE COSTS OF COMPLYING WITH SECTION 272, AND THE OI&M RESTRICTIONS IN PARTICULAR, ARE SUBSTANTIAL.

A. CLEC Claims That Section 272 Imposes Minimal Costs Are Inaccurate.

Some CLECs argue that the Section 272 requirements should be maintained because they impose minimal costs on BOC operations.⁵⁴ For example, WorldCom asserts that the Section 272 restrictions must not handicap BOCs because BOCs have gained market share at a greater rate than other new entrants.⁵⁵ AT&T claims that the costs of separate affiliates are "not at all prohibitive" based on the fact that BOCs often have more than one Section 272 affiliate.⁵⁶

⁵³ Texas PUC at 6.

⁵⁴ See, e.g., WorldCom at 7-10; AT&T at 46-48.

⁵⁵ WorldCom at 7.

⁵⁶ AT&T at 47-48.

These arguments are frivolous. SBC described the costs of structural separation in its comments, and the Commission itself, has long recognized that structural separation imposes significant costs on carriers and, by extension, society at large.⁵⁷ In fact, that is precisely why the BOCs' competitors want these requirements retained. Carriers that can integrate their local and long distance operations have an advantage over the BOCs, most critically in the provision of complex services to large business customers and in the ability to take advantage of new integrated equipment. Large business customers want seamless end-to-end services, with a single point of contact. The BOCs' competitors continue to hold an advantage in the long distance market place as long as BOCs are handicapped by 272 structural separation.

AT&T's argument that structural separation must not be costly because BOCs often have more than one Section 272 affiliate is similarly flawed. While SBC currently has more than one Section 272 affiliate, these affiliates were created because of past merger conditions. SBC relies primarily on one Section 272 affiliate, SBC Long Distance (SBCLD),⁵⁸ to provide in-region interLATA services, and the other affiliates are being phased out.⁵⁹ Moreover, the real costs of Section 272 are in the structural separation between the BOC and its long distance affiliate.

As the companies actually subject to the restrictions have explained in detail, structural separation imposes significant costs and burdens. To comply with Section 272, SBC must duplicate its resources, unlike its competitors. SBC estimates that it would save between 20 % and 75 % on different functions if it were able to integrate its local and long distance operations. Even more damaging, SBC is prohibited from using the latest equipment that integrates local and

⁵⁷ SBC at 5-6.

⁵⁸ Southwestern Bell Communications Services, Inc. ("SBCLD") is SBC's Section 272 affiliate authorized to provide in-region interLATA long distance in the SWBT region. As a result of the SBC/Ameritech merger, SBC acquired a Section 272 designated affiliate, Ameritech Communications Inc.("ACI"), and is in the process of integrating its operations into SBCLD.

⁵⁹ Although SBC will need to continue its Section 272 affiliate for its affiliated BOCs as the requirements sunset in others, the sunset will still provide significant benefits. The duplicative network planning and engineering costs will decrease; marketing will improve; and the BOC will be at less of at a competitive disadvantage vis-à-vis its competitors in providing end-to-end services, particularly in the business market.

long distance functions while its competitors are upgrading their networks, consequently, driving SBC's costs higher than its competitors.

SBC is faced with additional hurdles in the marketplace because it cannot provide seamless end-to-end services for its customers. For example, installation and repair is a multiple step process for SBC's separate affiliates, but can be done in one step by SBC's competitors. Other BOCs echo SBC's concerns. For example, Verizon has spent \$314 million "solely to meet the Section 272 separation requirements" and will spend another \$550 million through 2006. Verizon also notes that "[t]he costs of complying with separate affiliate rules divert capital from productive investments and development of innovative services." SBC's investment options are similarly limited by this competition for financial resources.

B. The OI&M Restrictions Are Unnecessary And Should Be Removed For All BOCs.

The prohibition on sharing OI&M services between the BOC and its long distance affiliate causes a substantial portion of the Section 272 costs. Without these restrictions, SBC would save approximately 50 % on personnel in network engineering, customer care, billing, and network operations. Verizon estimates that because of these restrictions, it will incur \$495 million in costs through 2006. More importantly, if BOCs and their Section 272 affiliates were allowed to share OI&M services, they would be able to provide end-to-end service for customers in almost the same manner as their competitors.

The OI&M restriction also hampers BOC efforts in the broadband market, which is relatively new and small in size. Broadband services are provided over platforms that integrate local and long distance voice and data services. As Verizon explained, "[t]he OI&M restriction

⁶⁰ SBC at 8-10.

⁶¹ Qwest at 13-15; BellSouth at 19.

⁶² Verizon at 10 (footnote omitted).

⁶³ Verizon at 11.

⁶⁴ Verizon at 17.

requires the use of multiple work groups to deal with arbitrarily delineated demarcations between 'local' and 'long distance' portions of what is technologically, as well as in the minds of customers, a single integrated end-to-end service." This duplicative approach hampers BOCs as they try to break into this market. These restrictions are not required by the statute, but rather were adopted by the Commission to ensure that the BOC and its affiliate operate independently. Experience has shown that the OI&M prohibition is not necessary to ensure independence prior to sunset. The Commission has already allowed sharing of administrative services because existing safeguards prevent discrimination and cross-subsidization. Sharing of OI&M services would be subject to these same protections. As explained above and confirmed by the Section 272 audits these and other safeguards are more than adequate to prevent anti-competitive behavior. Because of the costs these restrictions impose and the fact that they are neither necessary nor required by the statute, SBC supports Verizon's request that the Commission lifts the OI&M prohibition for all BOCs immediately. 66

VI. CONCLUSION.

The statutory language and legislative history demonstrate Congress's clear intent that Section 272 should sunset on a BOC-by-BOC basis three years after a BOC first obtains Section 271 authority in a state. Although numerous parties attempt to rewrite the statute by inserting a local competition market share test, there is no basis for adding such a requirement. Congress presumed that costly structural separation provisions would no longer be necessary three years after Section 271 authority was granted, and market conditions have proven this assumption correct. Continuing these requirements longer than required by the statute will only serve to put additional costs on the BOCs, hamper competition, and harm consumers. Other safeguards effectively prevent BOC discrimination and cross-subsidization, and state and federal regulators

⁶⁵ Verizon at 19.

⁶⁶ Verizon at 16-21.

will continue to have the authority they need to enforce the Act. Therefore, SBC urges the Commission to allow Section 272 to sunset three years after BOC interLATA entry in a state.

Respectfully submitted,

SBC Communications Inc.

By: /s/ Suzanne Yelen
SUZANNE YELEN

By: /s/ Terri L. Hoskins
TERRI L. HOSKINS
GARY L. PHILLIPS
PAUL K. MANCINI

WILEY REIN & FIELDING LLP 1776 K Street, NW Washington, D.C. 20006 (202) 719-7000 – phone (202) 719-7049 – facsimile

SBC COMMUNICATIONS INC. 1401 Eye Street, NW Suite 400 Washington, D.C. 20005 (202) 326-8893 – phone (202) 408-8763 – facsimile Its Attorneys

August 26, 2002

CERTIFICATE OF SERVICE

I, Regina Ragucci, do hereby certify that on this 26th day of August 2002, Reply Comments of SBC Communications Inc. in WC Docket No. 02-112, were served first class mail - pre-paid postage to the parties attached.

/s/ Regina Ragucci Regina Ragucci

LYNDA L. DORR
PUBLIC SERVICE COMMISSION OF
WISCONSIN
610 N. WHITNEY WAY
PO BOX 7854
MADISON, WI 53707-7854

MARC POSTON NATELLE DIETRICH MISSOURI PUBLIC SERVICE COMMISSION PO BOX 360 JEFFERSON CITY, MO 65102

DAVID L. LAWSON MICHAEL P. DOSS MICHAEL J. HUNSEDER SIDLEY AUSTIN BROWN & WOOD, LLP COUNSEL FOR AT&T CORP. 1501 K STREET, NW WASHINGTON, DC 20005

MARK C. ROSENBLUM LAWARENCE J. LAFARO ARYEH S. FRIEDMAN AT&T CORP. 295 NORTH MAPLE AVENUE BASKING RIDGE, NJ 07920

CHARLES H. HELEIN
JONATHAN S. MARASHLIAN
SUSAN CALLAGHAN
TOUCH AMERICA, INC.
130 N. MAIN STREET
BUTTE, MONTANA 59701

TERESA K. GAUGHLER JONATHAN ASKIN ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES 888 17TH STREET, NW WASHINGTON, DC 20005 SHARON J. DEVINE BLAIR A. ROSENTHAL QWEST SERVICES CORP. 1020 19TH STREET, NW SUITE 700 WASHINGTON, DC 20036

JOSEPH DIBELLA VERIZON 1515 NORTH COURTHOUSE ROAD SUITE 500 ARLINGTON, VA 22201

THOMAS JONES CHRISTI SHEWMAN WILKIE FARR & GALLAGHER COUNSEL FOR TIME WARNER TELECOM THREE LAFAYETTE CENTRE 1155 21ST STREET, NW WASHINGTON, DC 20036

PRAVEEN GOYAL COVAD COMMUNICATIONS COMPANY 600 14TH STREET, NW, SUITE 750 WASHINGTON, DC 20005

RICHARD J. METZGER FOCAL COMMUNICATIONS CORP. 7799 LEESBURG PIKE SUITE 850 NORTH FALLS CHURCH, VA 22043

JOHN SUMPTER
PAC-WEST TELECOMM, INC.
1776 MARCH LANE
SUITE 250
STOCKTON, CA 95207

WANDA MONTANO US LEC CORP. THREE MORROCROFT CENTRE 6801 MORRISON BLVD. CHARLOTTE, NC 28211 RICHARD M. RINDLER
PATRICK J. DONOVAN
PAUL O. GAGNIER
SWINDLER BERLIN SHEREFF FRIEDMAN,
LLP
COUNSLE FOR FOCAL COMM, PAC-WEST &
US LEC CORP.
3000 K STREET, NW, SUITE 300
WASHINGTON, DC 20007

LAWRENCE E. SARJEANT INDRA SEHDEV CHALK MICHAEL T. McMENAMIN ROBIN E. TUTTLE UNITED STATES TELECOM ASSOCIATION 1401 H STREET, NW SUITE 600 WASHINGTON, DC 20005

JONATHAN D. LEE
MAUREEN FLOOD
THE COMPETITIVE
TELECOMMUNICATIONS ASSOCIATION
1900 M STREET, NW
SUITE 800
WASHINGTON, DC 20002

ANGELA N. BROWN BELLSOUTH CORP. SUITE 4300 675 WEST PEACHTREE STREET, NE ATLANTA, GA 30375-0001 JOSE RIVERA-BENITEZ STATE OF NEW JERSEY DIVISION OF RATEPAYER ADVOCATE 31 CLINTON STREET, 11TH FLOOR PO BOX 46005 NEWARK, NJ 07101

ALAN BUZACOTT WORLDCOM, INC. 1133 19TH STREET, NW WASHINGTON, DC 20036 ROGER B. BORGELT
OFFICE OF ATTORNEY GENERAL STATE OF
TEXAS
CONSUMER PROTECTION DIVISION
PUBLIC AGENCY REPRESENTATION
SECTION
PO BOX 12548
AUSTIN, TX 78711-2548

NORINA MOY JAY C. KEITHLEY RICHARD JUHNKE SPRINT CORP. 401 9TH STREET, NW SUITE 400 WASHINGTON, DC 20004

CRAIG T. SMITH SPRINT CORP. 6450 SPRINT PARKWAY OVERLAND PARK, KS 66251 WASHINGTON UTILITIES & TRANSPORATION COMMISSION 1300 EVERGREEN PARK DRIVE, SW PO BOX 47250 OLYMPIA, WA 98504-7250 LAWRENCE G. MALONE STATE OF NEW YORK DEPARTMENT OF PUBLIC SERVICE THREE EMPIRE STATE PLAZA ALBANY, NY 12223-1350

STEVE ELLENBECKER STEVE FURTNEY KRISTIN H. LEE WYOMING PUBLIC SERVICE COMMISSION 2515 WARREN AVENUE SUITE 300 CHEYENNE, WY 82002

ROBERT S. TONGREN TERRY L. ETTER DAVID C. BERGMAN OHIO CONSUMERS' COUNSEL 10 WEST BROAD STREET, SUITE 1800 COLUMBUS, OH 43215

MICHAEL J. TRAVIESO MARYLAND PEOPLE'S COUNSEL SUITE 2102 6 ST. PAUL STREET BALTIMORE, MD 21202

NASUCA 8300 COLESVILEE ROAD SUITE 101 SILVER SPRING, MD 20910

REBECCA KLEIN BRETT A. PERLMAN PUBLIC UTILITY COMMISSION OF TEXAS 1701 N. CONGRESS AVENUE AUSTIN, TX 78711-3326 MARYANNE REYNOLDS MARTIN PENNSYLVANIA PUBLIC UTILITY COMMISSION 400 NORTH STREET PO BOX 3265 HARRISBURG, PA 17105-3265